

**Updated Informative Digest for**  
**Adoption of Proposed Amendments to California Code of Regulations,**  
**Title 18, Section 1618, *United States Government Supply Contracts***

On June 26, 2012, the State Board of Equalization (Board) held a public hearing on and unanimously voted to adopt the original text of the proposed amendments to California Code of Regulations, title 18, section (Regulation) 1618, *United States Government Supply Contracts*, described in the notice of proposed regulatory action. There have not been any changes to the applicable laws or the effect of the adoption of the proposed amendments to Regulation 1618 described in the informative digest included in the notice of proposed regulatory action. The Board did not receive any written comments regarding the proposed amendments to Regulation 1618 and no interested parties appeared at the public hearing on June 26, 2012.

The informative digest included in the notice of proposed regulatory action provides:

**“Current Regulation 1618**

“Unless an exemption applies, California imposes a sales tax on retailers, which is measured by their gross receipts from the retail sale of tangible personal property in California. (Rev. & Tax Code, § 6051.) As relevant here, RTC section 6007 provides that the term ‘retail sale’ means ‘a sale for any purpose other than resale in the regular course of business’ and RTC section 6381 provides an exemption from sales tax for gross receipts from the sale of tangible personal property to the United States.

“Regulation 1618 currently prescribes the circumstances under which a retailer may make non-taxable sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor who will resell the tangible personal property to the United States Government in the ordinary course of the contractor’s business (hereafter, ‘sales for resale to the United States’). The regulation generally provides that:

- A retailer’s sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are sales for resale to the United States if the United States takes title to the tangible personal property pursuant to a United States Government supply contract prior to the time the contractor uses the property to perform the function or act for which the property was designed or manufactured; and
- A retailer’s sales of tools, equipment, direct consumable supplies, and overhead materials to a United States Government supply contractor are not sales for resale to the United States if the contractor makes any use of the property to perform the function or act for which the property was designed or manufactured prior to the time that title to the property passes to the United States.

“Regulation 1618 also currently provides specific guidance for determining when title to direct consumable supplies and overhead materials passes to the United States under a United States Government supply contract. In addition, the United States Government has uniform acquisition policies and procedures for its executive agencies, which are codified in the FAR, and Regulation 1618 provides specific guidance as to when title to ‘special tooling’ passes to the United States under the FAR.

#### “2007 Amendments to FAR

“Regulation 1618 was last amended in 1995 to provide specific guidance for determining when title to overhead materials passes to the United States in accordance with the Court of Appeal’s decision in *Aerospace Corporation v. State Board of Equalization* (1990) 218 Cal.App.3d 1300, and when title to ‘special tooling’ passes to the United States in accordance with FAR part 52.245-17. However, the federal government amended the FAR in 2007, and, among other changes, repealed FAR part 52.245-17, which contained special title passage clauses applicable to contracts for ‘special tooling,’ and consolidated a number of clauses regarding the passage of title to the federal government into FAR part 52.245-1, effective June 14, 2007.

#### “Effect, Objectives, and Benefits of the Proposed Amendments to Regulation 1618

“The Board directed its staff to meet with interested parties to discuss whether Regulation 1618 needs to be amended due to the repeal of FAR part 52.245-17 and any other changes in United States Government supply contracts. At the conclusion of the interested parties process, Board staff prepared Formal Issue Paper 12-001, which raised the issue of whether the Board should amend Regulation 1618 to conform to changes in the FAR, and recommended that the Board amend Regulation 1618 to:

- Delete the provisions in subdivision (a)(2) providing that the term ‘tools,’ as used in the definition of direct consumable supplies, does not include ‘special tooling’;
- Add new provisions to subdivision (a)(2) specifying that, effective June 14, 2007, the term ‘tools,’ as used in the definition of direct consumable supplies, includes ‘special tooling’ that ‘was previously covered by FAR part 52.245-17’; and
- Amend the second to last sentence in subdivision (b) to reflect that the FAR’s title passage clauses for special tooling applied until Jun 13, 2007, but were no longer effective after that date.

“In addition, Formal Issue Paper 12-001 recommended that the Board amend Regulation 1618, subdivision (a)(3) to clarify that costs for ‘overhead materials’ must be allocated to United States Government supply contracts ‘consistent with government cost accounting standards.’ It also recommended that the Board clarify the guidance provided in subdivision (b) regarding the passage of title to ‘direct consumable supplies’ and ‘overhead materials’ by separating subdivision (b) into paragraphs (1) through (3), explaining that overhead materials are one example of ‘indirect consumable supplies,’ and providing distinct guidance regarding the passage of title to direct consumable

supplies, which are directly reimbursable under specific contracts, and indirect consumable supplies, which must be allocated to specific contracts.

“The Aerospace Industries Association (AIA) participated in Board staff’s meetings with the interested parties and AIA agreed with staff’s recommended amendments to Regulation 1618 as set forth in Formal Issue Paper 12-001.

“During its March 20, 2012, Business Taxes Committee meeting, the Board determined that staff’s recommended amendments are reasonably necessary to accomplish the objectives of making Regulation 1618 consistent with the 2007 amendments to the FAR and clarifying Regulation 1618’s guidance regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials. The proposed amendments are anticipated to provide the following specific benefits:

1. Ensure that Regulation 1618 is consistent with the amendments made to the FAR effective June 14, 2007;
2. Eliminate confusion regarding the treatment of special tooling after the 2007 amendments to the FAR;
3. Explain that overhead materials are one example of indirect consumable supplies; and
4. Provide more certainty regarding sales for resale to the United States of direct consumable supplies and indirect consumable supplies, including overhead materials.

“The Board has performed an evaluation of whether the proposed amendments to Regulation 1618 are inconsistent or incompatible with existing state regulations and determined that the proposed amendments are not inconsistent or incompatible with existing state regulations because Regulation 1618 is the only state regulation prescribing the requirements for making sales for resale to the United States. In addition, there is no federal sales tax and there are no comparable federal regulations or statutes to Regulation 1618.”